

ORIGINAL

Before the  
FEDERAL COMMUNICATIONS COMMISSION  
Washington, D.C. 20554

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In the Matter of )  
 )  
Market Entry and Regulation of ) IB Docket No. 95-22  
Foreign-affiliated Entities ) RM-8355  
 ) RM-8392

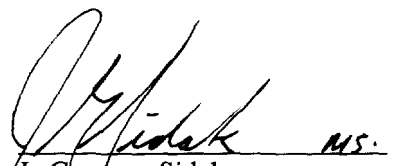
FEDERAL COMMUNICATIONS  
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REPLY COMMENTS OF J. GREGORY SIDAK

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In the notice of proposed rulemaking in this docket, the Commission has proposed that its approval of foreign investment under section 310(b) of the Communications Act should depend, in part, on the extent to which the telecommunications sectors of the foreigner's home market and other primary markets are open to investment by Americans. To assess whether the Commission's proposal would succeed in opening foreign telecommunications markets to American investment, one must first marshal, for each of the world's key telecommunications markets, the facts concerning the current level of American investment and the current regulatory policy on foreign investment. Such an analysis for selected countries is provided in the report attached to these comments. The report is a draft chapter of a book that I am writing on foreign investment in telecommunications.

Respectfully submitted,

  
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May 12, 1995

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# American Telecommunications Investment in Selected Overseas Markets

J. Gregory Sidak

May 12, 1995

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## American Investment Abroad

AMERICAN INVESTMENT in foreign telecommunications markets is often precluded by regulation in the given foreign country. Despite an accelerating trend of privatization and liberalization, most nations maintain a government-owned telecommunications monopoly. Foreign direct investment in the telecommunications markets of these countries is typically prohibited or regulated—either through an express statutory limitation on foreign investment, implicitly through a limitation on the number of available telecommunications operator licenses, or through a system in which an applicant for a new telecommunications operating license will be rejected solely because it is a consortium that has a significant foreign investor. As a result of these various means of exclusion, the extent of American direct investment in telecommunications services markets around the world has reflected the perceived need in individual countries for American technology and operating expertise. For that reason, American direct investment in most European markets, the United Kingdom aside, has been almost entirely in the wireless sector of the industry, whereas in South America for example, American direct investment has taken place not only in wireless, but also in the less developed wire-based industry.

This chapter surveys the telecommunications markets in countries from different regions around the world. The analysis begins with an examination of the markets belonging to America's trading partners under the North American Free Trade Agreement (NAFTA)—Canada and Mexico. We then examine selected members of the European Union, the varying market structures in certain Asian/Pacific countries, and the change occurring in several significant South American countries.

The analysis for most countries in each of these regions reveals a recurring theme: The foreign country opens certain sectors of its telecommunications industry to foreign investment only to the limited extent that country's government deems necessary. Typically, foreign telecommunications firms either acquire a minority stake in

## 2 *Foreign Investment in Telecommunications*

an existing domestic operator or assume a minority interest in a joint venture with a large domestic company having abundant financial resources, cultural understanding, and political clout but lacking telecommunications expertise. Foreign telecommunications firms have been willing to trade their technological expertise and marketing experience for a minority interest in the telecommunications operator because they believe that once they can get a “strategic foothold”—as AirTouch dubbed its equity participation in the Japanese wireless market<sup>1</sup>—they will then have the ability to leverage that limited interest to a more pervasive participation in that country’s telecommunications industry.

In turn, the strategic footholds of American telecommunications firms in foreign markets are likely to facilitate the formation of a number of competing full-service networks that compete on a global scale, the first such networks being AT&T and the alliance between BT and MCI.<sup>2</sup> A super carrier of this sort would take over all the telecommunications services for a huge international firm, such as GM, freeing it to concentrate on making cars. The carrier would establish a virtual private network to handle voice mail. It would also provide a single billing system, probably outsourcing services such as local calling to a regional carrier.<sup>3</sup>

1. AIRTOUCH COMMUNICATIONS, INC., 1994 ANNUAL REPORT 64 (1995).

2. Julia Flynn, Catherine Arnst & Gail Edmondson, *Who’ll Be the First Global Phone Company?*, BUS. WK., Mar. 27, 1995, at 176.

3. UNIVERSITY OF COLORADO INTERDISCIPLINARY TELECOMMUNICATIONS PROGRAM, TELECOMMUNICATIONS DATABASE REPORT, at 2-18 (1994).

## AMERICA'S NAFTA PARTNERS

### *Mexico*

In 1990, Mexico began a six-year process of privatization and liberalization of its telecommunications sector. Despite the progress that has been made so far during this period, foreign direct investment in the Mexican telecommunications industry remains relatively limited. The government maintains a 49 percent cap on foreign equity ownership, and, other than a minority interest held by France Telecom and SBC Communications in Teléfonos de México, S.A. de C.V. (Telmex), the former state-owned public telecommunications operator, most of the foreign investment in Mexican telecommunications as of 1995 is confined to the wireless sector. With the imminent expiration of Telmex's monopoly and the prime growth conditions that exist in Mexico's telecommunications industry, however, many potential entrants are poised to participate in the Mexican market.

Although chastened by the peso's devaluation in 1994 and 1995, the growth of the Mexican telecommunications market over the next two decades is expected to be substantial because of three factors: NAFTA, a relatively underdeveloped national telecommunications infrastructure, and rising per capita income. The telecommunications services market in Mexico currently generates over \$7 billion in annual revenue; by 2000, that number is expected to reach nearly \$20 billion.<sup>4</sup> The long-distance telephony market alone is expected to grow by 12 to 22 percent annually for several years.<sup>5</sup> But even with communications revenues expected to grow so rapidly, the line penetration rate in Mexico remains relatively low. Mexico has a population of 92 million people, but only 9.2 telephone lines per 100 people.<sup>6</sup> These factors, along with the expectation that

4. Ted Bardacke, *Sprint links with Telmex and cancels Iusacell deal*, FIN. TIMES, Dec. 15, 1994, at 35.

5. Ted Bardacke, *Tough times for Telmex as Mexico prepares to open market—Dominant position threatened as telecoms company faces increasing competition without a big partner*, FIN. TIMES, Nov. 17, 1994, at 28 [hereinafter *Tough times for Telmex*].

6. INTERNATIONAL TELECOMMUNICATIONS UNION, WORLD TELECOMMUNICATION DEVELOPMENT 64 (1994) [hereinafter ITU WORLD DEVELOPMENT REPORT]; DILLON, READ & CO. INC., TELÉFONOS DE MÉXICO: ONE OF THE SURVIVORS 4 (Feb. 27, 1995)

#### 4 *Foreign Investment in Telecommunications*

international telephony traffic originating or terminating in Mexico will increase significantly because of the growing presence of multinational firms (particularly American firms) in Mexico, make the Mexican telecommunications markets an attractive opportunity for direct investment by foreign telecommunications firms.<sup>7</sup>

*Telephony.* The Mexican Law on General Means of Communication (Communications Law), adopted in 1940, and the Telecommunications Regulations, adopted thereunder in October 1990, govern the telecommunications industry in Mexico.<sup>8</sup> This statute and the corresponding regulations authorize the Secretaría de Comunicaciones de México (SCT) to administer and enforce the regulation of the industry.<sup>9</sup> Under the Communications Law and the Telecommunications Regulations, any entity wishing to provide public telecommunications services must first receive a concession granted by the SCT.<sup>10</sup>

Mexico restricts foreign ownership of a telecommunications operator in the following manner. Under the Communications Law and the Telecommunications Regulations, the SCT may grant a concession only to a Mexican citizen or corporation, and the concessionaire may not transfer or assign the concession without the SCT's approval.<sup>11</sup>

Under the 1993 Foreign Investment Law and the 1989 Regulations adopted under the predecessor law, non-Mexican investors may not own more than 49 percent of the capital stock of a Mexican corporation operating in certain economic sectors, including telephone services.<sup>12</sup> The holdings of non-Mexican investors, however, may qualify as Mexican-owned if held through a trust that meets certain conditions to ensure that the non-Mexican investors

(written by Cynthia L. Rix).

7. Bardacke, *Tough times for Telmex*, *supra* note \_\_\_, at 28.

8. TELÉFONOS DE MÉXICO, S.A. DE C.V., 1993 SEC FORM 20-F, at 1 (1994).

9. Oscar M. Garibaldi & Raidza M. Torres, *Recent Developments in the Telecommunications Market in Canada, Latin America and the Caribbean*, in FEDERAL COMMUNICATIONS BAR ASSOCIATION, INTERNATIONAL PRACTICE COMMITTEE, 1993 INTERNATIONAL COMMUNICATIONS PRACTICE HANDBOOK 251, 253 (Paul J. Berman & Ellen K. Snyder eds., 1993).

10. TELÉFONOS DE MÉXICO, S.A. DE C.V., 1993 SEC FORM 20-F, at 9 (1994).

11. *Id.* at 9.

12. *Id.* at 17.

do not determine how their shares are voted. Therefore, non-Mexican investors may own a majority of the telecommunications operator's voting stock if such ownership is held in a trust that effectively neutralizes the votes of the non-Mexican investors.<sup>13</sup> An acquisition of shares by a non-Mexican investor in violation of the foreign investment restrictions voids any rights that the shareholder would have with respect to the violative shares. It would appear that this draconian sanction would even take away the investor's right to sell his shares, let alone his right to receive dividends. Unlike the American rule, such a violation in no way affects the concessionaire.<sup>14</sup>

A further protective measure applies only to the ownership of Telmex. Both the Foreign Investment Law and Telmex's concession ensure that non-Mexican investors do not achieve administrative control and management of the company.<sup>15</sup> Any violation of this restriction will void Telmex's concession.<sup>16</sup>

To ensure greater government control during times of crisis, the Communications Law gives certain rights to the Mexican government in its relations with concessionaires, including the right to assume the management and control in cases of imminent danger to national security or the national economy. The government exercised this power most recently in 1986 to ensure continued service during labor disputes.<sup>17</sup>

Finally, under the Communications Law and Telmex's bylaws, foreign states are prohibited from directly or indirectly owning shares of Telmex. Telmex has three classes of stock: AA, A, and L. The AA shares have full voting rights; the A and L shares do not. State-owned enterprises, such as France Telecom, organized as separate entities with their own assets, may own minority interests in Telmex's full-voting AA shares and may own an unlimited number of its limited-voting L and A shares.<sup>18</sup>

13. *Id.* at 18.

14. *Id.* at 18.

15. *Id.* at 18.

16. *Id.* at 18.

17. *Id.* at 9.

18. *Id.* at 18.

## 6 *Foreign Investment in Telecommunications*

As of 1995, Telmex holds the only license to supply fixed-link telecommunications services in Mexico.<sup>19</sup> Telmex provides basic telephone service, consisting of international and domestic long-distance, local service, and cellular mobile telephone service.<sup>20</sup> Until 1990, Mexico maintained Telmex as the state-owned monopoly telecommunications operator. In December of that year, the Mexican government began the privatization of Telmex by selling a 20.4 percent interest to a consortium consisting of SBC Communications Inc. (one of the seven American Regional Bell Operating Companies then called Southwestern Bell Corporation), France Telecom (the state-owned French telecommunications operator), and a group of Mexican investors led by Grupo Carso, S.A. de C.V.<sup>21</sup> The consortium has voting control of Telmex; the Mexican investors have voting control of the consortium.<sup>22</sup>

In 1990, Mexico's National Commission on Foreign Investment, the regulatory body responsible for administering the Foreign Investment Law and Regulations, ruled that Telmex's L shares were not subject to, and were not considered when determining compliance with, the foreign ownership restriction because the shares have only limited voting rights.<sup>23</sup> The A shares are similarly unrestricted.<sup>24</sup> To ensure that its privatization of Telmex fell within the foreign ownership constraints while allowing for some infusion of foreign capital and telecommunications expertise, the Mexican government sold 100 percent of the AA shares, constituting voting control of Telmex and representing 20.4 percent of Telmex's entire capital stock, to a trust for the benefit of the consortium mentioned above: SBC and France Telecom each own 24.5 percent of the AA shares; Grupo Carso owns 25.3 percent; Seguros de Mexico, S.A. owns 2.9 percent; two other investors each own 3 percent; and 48 other investors, none with more than 1.8 percent of the AA shares, own the remainder. Carlos Slim Helu, one of Mexico's wealthiest citizens,

19. *Id.* at 8.

20. *Id.* at 1.

21. SOUTHWESTERN BELL CORPORATION, 1993 SEC FORM 10-K, at 9 (1994).

22. SOUTHWESTERN BELL CORPORATION, 1993 ANNUAL REPORT 42 (1994).

23. TELÉFONOS DE MÉXICO, S.A. DE C.V., 1993 SEC FORM 20-F, at 17 (1994).

24. *Id.* at 17.

controls both Grupo Carso and Seguros de Mexico; together, the two companies own 28.2 percent of Telmex's AA shares.<sup>25</sup>

In 1991 and 1992, the Mexican government executed, on both the Mexican and international stock exchanges, two public offerings of the Telmex shares it still held, primarily the L shares.<sup>26</sup> In addition, SBC exercised an option in September 1991 to purchase a block of L shares.<sup>27</sup> SBC's total interest now represents approximately 10 percent of Telmex's total equity capitalization.<sup>28</sup> The Mexican government retains 2.1 percent of the L shares, or 1.6 percent of the total capital stock of the company.<sup>29</sup> The unrestricted shares that are traded on foreign exchanges amount to a significant portion of Telmex's total outstanding stock. Approximately 60 percent of the company's total capital stock is held by foreigners, mostly Americans.<sup>30</sup>

To attract significant foreign investment and to ensure a certain level of infrastructure development, the Mexican government granted Telmex the only license to operate fixed-link telecommunications services in Mexico,<sup>31</sup> a statutory monopoly over domestic and international telephone service until August 1996,<sup>32</sup> and a statutory monopoly over local telephone service until 2026.<sup>33</sup> Under the Communications Law and the Telecommunications Regulations, no competing provider of fixed-link domestic or international long-distance services may operate before August 1996. Thereafter, the SCT may grant concessions to other long-distance carriers. After December 31, 1996, Telmex must permit other long-distance telephone networks to interconnect with Telmex's extensive network in a manner that enables customers to choose the network by which their calls are carried.<sup>34</sup>

25. *Id.* at 14.

26. INTERNATIONAL TELECOMMUNICATIONS UNION, *supra* note \_\_\_, at 64.

27. SOUTHWESTERN BELL CORPORATION, 1993 ANNUAL REPORT 42 (1994).

28. SBC COMMUNICATIONS INC., 1994 SEC FORM 10-K, at 6 (1995).

29. TELÉFONOS DE MÉXICO, S.A. DE C.V., 1993 SEC FORM 20-F, at 13 (1994).

30. Anthony DePalma, *Telmex in Competition, So Far With Just Itself*, N.Y. TIMES, July 18, 1994, at D1.

31. DILLON, READ & CO., INC., *supra* note \_\_\_, at 2.

32. SBC COMMUNICATIONS INC., 1994 ANNUAL REPORT 30 (1995).

33. Claudia Fernandez, *What's on Line for the Future*, BUS. MEXICO, Jan./Feb. 1995, at 3.

34. TELÉFONOS DE MÉXICO, S.A. DE C.V., 1993 SEC FORM 20-F, at 11 (1994).

In July 1994, the SCT issued the first of several rules that will govern the advent of competition in the Mexican long-distance market. The rule stated that there will be an unlimited number of concessions and that Telmex shall provide 60 points of interconnection by January 1, 1997 and over 200 points of interconnection by 2000.<sup>35</sup> On April 24, 1995, the SCT sent a bill to the Mexican Congress defining many of the terms upon which entrants will be allowed into the Mexican telecommunications markets.<sup>36</sup> SCT Secretary Carlos Ruiz Sacristan announced that, under the proposed bill, entrant firms will not have to pay a concession fee to compete with Telmex but will have to pay a fee to use radio spectrum.<sup>37</sup> The bill makes no distinction between local and long-distance service.<sup>38</sup>

The SCT, however, has made no announcement regarding three other important issues surrounding the introduction of competition: the pricing of interconnection by entrant firms with Telmex's network;<sup>39</sup> whether the new firms will have any external obligations such as the provision of universal service; and how, if at all, the government will regulate tariffs.<sup>40</sup> While the SCT has delayed announcing its policies concerning these remaining issues for long-distance competition, industry sources predict that the SCT will set forth the remaining rules by the middle of 1995.<sup>41</sup> A senior Mexican official announced in April 1995 that the government will try to encourage greater competition in the local telephone market before the expiration in 2026 of Telmex's statutory monopoly over local services.<sup>42</sup>

With the announcement that it will not charge licensing fees for potential entrants to the telecommunications market, the Mexican government signalled the importance that it places on developing the nation's telecommunications system and on using competition to spur

35. SBC COMMUNICATIONS INC., 1994 SEC FORM 10-K, at 30 (1995).

36. Martin Langfield, *Mexico bill sets terms of telecomm liberalization*, REUTERS, Apr. 25, 1995.

37. Paul B. Carroll, *Mexico Rejects Phone-Market Entry Fees*, WALL ST. J., Apr. 12, 1995, at A11.

38. Langfield, *Mexico bill sets terms of telecomm liberalization*, *supra* note \_\_.

39. Carroll, *Mexico Rejects Phone-Market Entry Fees*, *supra* note \_\_, at A11.

40. Damian Fraser, *Mexico in telephone liberalisation*, FIN. TIMES, July 4, 1994, at 23.

41. Fernandez, *What's on Line for the Future*, *supra* note \_\_, at 2.

42. DILLON, READ & CO., INC., *supra* note \_\_, at 7.

this development. With the devaluation of the peso and the nation's resultant liquidity crunch, the Mexican government faced pressures to exact a high concession fee from market entrants. The government resisted these pressures, however, acknowledging that sophisticated telecommunications infrastructure and services are important not only as a final good, but also as a vital input for other sectors of a nation's economy. The Mexican government reinforced its position that competition is the best way to develop Mexico's telecommunications industry.

As the uncertainty surrounding the future of Mexico's long-distance telephony market abates, many potential entrants stand waiting because of the extraordinary opportunity involved. In 1993, Mexican international and domestic long-distance services generated approximately \$4.2 billion;<sup>43</sup> this market is expected to grow to nearly \$12 billion by the end of the decade. In addition to the opportunity inherent in such growth, potential entrants are drawn by the chance to undercut the former state-owned monopoly incumbent, and "cream-skim" its most lucrative markets.

Telmex's costs and prices are high. In consideration for the ward of its monopoly concession, Telmex had to (1) expand service at an average annual rate of 12 percent through 1994; (2) reduce the waiting period for service and repairs; (3) improve the quality of service; and (4) install one telephone line in every town of over 500 inhabitants by 1994.<sup>44</sup> As one of the country's largest non-government employers, with a labor force of nearly 63,000 employees, Telmex cannot easily reduce its costs as it faces real or imminent competition. Furthermore, Telmex relies upon its disproportionately high revenues earned from its international and domestic long-distance services to subsidize the costs of local telephone service, the mandatory infrastructure buildout, and the improved service requirements.<sup>45</sup> Despite its high costs, Telmex earns profit margins of 43 percent (among the highest in the world).<sup>46</sup> suggesting that there exists a

43. HANCOCK INSTITUTIONAL EQUITY, INVESTING IN THE "EMERGING" TELECOMMUNICATIONS INDUSTRY 24 (Dec. 2, 1994) (written by Douglas C. Ashton).

44. TELÉFONOS DE MÉXICO, S.A. DE C.V., 1993 SEC FORM 20-F, at 4 (1994).

45. Paul B. Carroll, *Mexico Rejects Phone-Market Entry Fees*, *supra* note \_\_\_, at A11.

46. John J. Keller & Craig Torres, *AT&T Corp. and Grupo Alfa Plan Venture*, *WALL ST. J.*, Nov. 10, 1994, at A6.

significant opportunity for competitors to underprice Telmex while still earning a healthy return on investment.

To gain a share of this large and growing market, the three largest American long-distance firms (AT&T, MCI, and Sprint), the largest American independent telecommunications firm (GTE), and another RBOC (Bell Atlantic) have all formed alliances with large Mexican companies.

In November 1994, AT&T announced a \$1 billion joint venture with Grupo Industrial Alfa, S.A. (Grupo Alfa).<sup>47</sup> AT&T will own 49 percent; Grupo Alfa will own 51 percent. The two companies intend to invest \$1 billion by 1998 or 2000.<sup>48</sup> The joint venture will first focus on the business market for local and long-distance, and then it will gradually extend services to residential subscribers.<sup>49</sup> Grupo Alfa is one of Mexico's largest industrial corporations, with 22,500 employees and \$2.49 billion in sales in 1993.<sup>50</sup> With its new partner, AT&T gains not only significant financial might and a strong knowledge of Mexican business, but also the political influence of one of Mexico's wealthiest industrial families, the Garzas of Monterrey.

In January 1994, MCI announced plans to build a long-distance network in Mexico with Grupo Financiero Banamex Accival (Banacci).<sup>51</sup> Banacci, Mexico's largest banking company, will own 55 percent of the joint venture; MCI will own 45 percent. Over the next three years the two companies intend to spend \$1 billion to build a fiber optic long-distance network between Mexico City, Monterrey, and Guadalajara.<sup>52</sup> The joint venture thus will target the most lucrative portion of the Mexican market, for 45.8 percent of all

47. Anthony DePalma, *AT&T Gets Mexico Partner for Long-Distance Service*, N.Y. TIMES, Nov. 10, 1994, at D1.

48. Damian Fraser, *AT&T in Mexican joint venture*, FIN. TIMES, Nov. 10, 1994, at 25.

49. Keller & Torres, *AT&T Corp. and Grupo Alfa Plan venture*, *supra* note \_\_\_, at A6.

50. DePalma, *AT&T Gets Mexico Partner for Long-Distance Service*, *supra* note \_\_\_, at D1.

51. Damian Fraser, *Rivals target Mexican monopoly—Telmex is to face competition for the first time*, FIN. TIMES, Jan. 7, 1994, at 34.

52. Edmund L. Andrews, *MCI Joins Mexican Phone Venture*, N.Y. TIMES, Jan. 26, 1994, at D3.

telephone access lines in Mexico are concentrated in those three cities.<sup>53</sup>

Sprint formed an alliance with Telmex in December 1994 to provide telecommunications services throughout North America, cancelling an agreement between Sprint and Iusacell.<sup>54</sup> Sprint and Telmex will not form a new entity, but will exchange products and services, including software platforms and other intellectual property.<sup>55</sup>

GTE agreed in September 1994 to form a joint venture with Grupo Financiero Bancomer (Bancomer), Mexico's second largest financial group, and Valores Industriales (VISA), an industrial conglomerate.<sup>56</sup> The joint venture will provide long-distance services to business customers. GTE will own 49 percent; the two Mexican companies together will own 51 percent.<sup>57</sup>

As will be described in greater detail below, Bell Atlantic has a 42 percent interest in Iusacell, Mexico's largest independent cellular provider. As of 1995, Iusacell has provided only cellular service, but the company now intends to offer basic local telephone service over a wireless network.<sup>58</sup> Iusacell already has a license to build a fixed wireless local telephone network<sup>59</sup> and concessions covering three-fourths of the Mexican population.<sup>60</sup> With the advent of long-distance competition in Mexico in the near future and the recent permission granted the RBOCs under the Modification of Final Judgment to offer long-distance service to their wireless customers,<sup>61</sup> Iusacell stands as another likely bidder for a long-distance concession.

53. TELÉFONOS DE MÉXICO, S.A. DE C.V., 1993 SEC FORM 20-F, at 4 (1994).

54. Ted Bardacke, *Sprint links with Telmex and cancels Iusacell deal*, *supra* note \_\_\_, at 35.

55. *Id.* at 35.

56. Damian Fraser, *GTE agrees Mexican telephone venture*, FIN. TIMES, Sept. 28, 1994, at 34.

57. *GTE to Enter Mexico Market*, N.Y. TIMES, Sept. 28, 1994, at D2.

58. Damian Fraser, *Rivals target Mexican monopoly-Telmex is to face competition for the first time*, *supra* note \_\_\_, at 34.

59. Craig Torres, *Telmex Monopoly to Face Fight From Wealthy Mexican Investor*, WALL ST. J., May 3, 1994, at A10.

60. HANCOCK INSTITUTIONAL EQUITY, *supra* note \_\_\_, at 23.

61. Leslie Cauley, *Seven Baby Bells Win Right to Provide Long-Distance to Cellular Customers*, WALL ST. J., May 1, 1995, at B4.

Finally, the last of the notable companies that has already positioned itself as a potential entrant to the Mexican telecommunications industry, Grupo Pulsar, S.A. de C.V. (Pulsar), also intends to provide local telephone service over a fixed wireless network.<sup>62</sup> Alfonso Romo Garza, chairman and chief executive of Pulsar, purchased a 15 percent stake in Ionica, the private British telecommunications company pioneering radio access. Ionica intends to offer a local telephone service for “fixed” phones to compete with BT, Mercury, and the cable companies.<sup>63</sup> Pulsar’s strategic partnership secures for it the licensing rights to the technology for Mexico and a “priority” for all Latin American countries.<sup>64</sup> Fixed wireless networks are less complicated and less expensive than cellular networks, and they can be installed more quickly and at lower cost than a wire-based telephone network.

*Wireless.* In 1989, the SCT liberalized the Mexican cellular market. The regulatory body authorized two cellular licenses (A-band and B-band) in each of nine regions in Mexico. The SCT auctioned off the A-band licenses, and it gave the B-band licenses to Radiomovil Telcel (Telcel), Telmex’s wholly owned cellular subsidiary. The Mexican cellular market has subsequently grown to approximately 435,000 subscribers, the largest cellular market in Latin America.<sup>65</sup> Rates for cellular services are regulated under the respective separate concessions.<sup>66</sup> The foreign ownership restrictions described above apply to cellular operators as well.

Telcel is the only company in Mexico licensed to provide nationwide cellular mobile telephone services. Telcel competes in each region with one other cellular operator holding a regional concession. The competitors provide nationwide cellular service through a cooperative arrangement.<sup>67</sup> Telcel has about 50 percent of the market.

62. Torres, *Telmex Monopoly to Face Fight From Wealthy Mexican Investor*, *supra* note \_\_\_, at A10.

63. *Mexico link helps Ionica raise Pounds 30m*, FIN. TIMES, June 2, 1994, at 24.

64. Torres, *Telmex Monopoly to Face Fight From Wealthy Mexican Investor*, *supra* note \_\_\_, at A10.

65. Fernandez, *What’s on Line for the Future*, *supra* note \_\_\_, at 14.

66. TELÉFONOS DE MÉXICO, S.A. DE C.V., 1993 SEC FORM 20-F, at 6 (1994).

67. *Id.* at 6.

Iusacell is Mexico's second largest telecommunications company and the country's largest independent cellular operator.<sup>68</sup> The company owns licenses in four of the nine regions, covering two-thirds of Mexico and more than 60 million potential subscribers (POPs).<sup>69</sup> Bell Atlantic owns 41.9 percent of Iusacell's total equity; the holding constitutes a 44 percent voting interest.<sup>70</sup> Bell Atlantic purchased the stake for a total of \$1.04 billion.<sup>71</sup>

In 1994, Motorola acquired a 42 percent interest in Baja Celular for \$100 million.<sup>72</sup> The stake in Baja Celular gives Motorola an equity interest in the four cellular companies that cover the 2,000-mile border between the U.S. and Mexico and all of Northern Mexico. Motorola has stakes in the two cellular companies that cover northeast Mexico, while Baja Celular (and its fully-owned subsidiary, Mobitel) cover the northwest.<sup>73</sup> Grupo Protexa, a Mexican industrial company, also invested in Baja Celular. Motorola has announced that it will form a new venture with Grupo Protexa that would acquire Motorola's cellular interests and invest \$1.5 billion in Mexican telecommunications.<sup>74</sup> The new company will participate in the auctions for a long-distance concession.

In 1990, BellSouth won a cellular concession for Guadalajara and the surrounding area. BellSouth then formed Communications Celulares de Occidente S.A. de C.V. (Occidente) as the operator to provide the cellular service. BellSouth held a 30 percent interest in the company but sold that stake to Iusacell in 1994.<sup>75</sup>

*Cable Television.* Cable television networks in Mexico are relatively undeveloped, and the penetration rate of cable television service is very low. Only about 1.3 million of the 16 million Mexican house-

68. BELL ATLANTIC, 1994 ANNUAL REPORT 5 (1995).

69. *Id.* at 5.

70. *Id.* at 5; *Bell Atlantic Completes Purchase of Iusacell Stake*, N.Y. TIMES, Aug. 12, 1994, at D3.

71. *Bell Atlantic Completes Purchase of Iusacell Stake*, *supra* note \_\_\_, at D3.

72. Damian Fraser, *Motorola invests in Mexican cellular group*, FIN. TIMES, June 24, 1994, at 25.

73. *Id.* at 25.

74. *Id.* at 25.

75. *BellSouth Ends Tie to Mexico Cellular Provider*, N.Y. TIMES, Feb. 5, 1994, at 39.

## 14 *Foreign Investment in Telecommunications*

holds with a television subscribe to a cable television service.<sup>76</sup> For the same reasons cited for the expected growth in telephony, the cable television market in Mexico is expected to grow at the high rate of 25 percent annually through 2000.<sup>77</sup> Again, the foreign ownership restrictions on telecommunications outlined above apply to cable television networks.

Televisa is Mexico's largest media company. Cablevision is the cable television arm of Televisa. Cablevision has 220,000 subscribers. In 1994, Telmex agreed to purchase 49 percent of Cablevision for \$211 million.<sup>78</sup> The relationship created by Telmex's equity interest would enable Cablevision to expand its television service using Telmex's fiber optic network and would help Telmex provide video and data services. Telmex's concession explicitly prohibits Telmex from using "directly or indirectly, any concession for public television services." Nevertheless, Telmex argues that this provision does not prevent it from carrying Cablevision's signal on its network. Telmex is confident that it will receive regulatory approval.<sup>79</sup>

In 1995, C-TEC, a small cable television and telephone subsidiary of the American heavy construction conglomerate, Peter Kiewit Sons' Inc., agreed to purchase for \$84 million 40 percent of Mexico's second largest cable television company, Megacable.<sup>80</sup> C-TEC provides cable television service in New York and Michigan and long-distance telephone service in Pennsylvania and New England.

### *Canada*

Until recently, ten telecommunications operators had a monopoly on the provision of basic telecommunications services in Canada. Each company provided local telephone services, on an exclusive basis, within its own region. Together they provided long-distance services, also on an exclusive basis. The Canadian government, however, has

76. *Id.* at 5.

77. *Id.* at 5.

78. Damian Fraser, *Telmex seeks 49% stake in cable-TV business*, FIN. TIMES, Dec. 1, 1994, at 30.

79. *Id.* at 31.

80. Steven Lipin, *U.S. Cable-TV Firm To Buy a 40% Stake in Mexican Company*, WALL ST. J., Jan. 25, 1995, at A3.

initiated a reform of its telecommunications regulatory policy, using competitive market forces to shape the next generation of Canada's telecommunications industry.<sup>81</sup> The Canadian government introduced competition to the cellular telephony market in 1985 and to the long-distance telephony market in 1992.<sup>82</sup> In 1994, the Canadian government decided to allow competition in the market for local switched voice telephony.<sup>83</sup> In all but the cellular market, actual competition is not yet pervasive, but the benefits of the more competitive regime have already become apparent.

The telecommunications services industry in Canada is large and well developed. Canada has a population of 27.4 million people.<sup>84</sup> Over 99 percent of Canadian homes have at least one telephone and receive telephone services.<sup>85</sup> In 1992, Canada had 59.21 telephone lines per 100 inhabitants, compared to 56.49 in the United States.<sup>86</sup> In 1994, telecommunications services in Canada generated over \$13.4 billion; by 2000, that number is expected to exceed \$17.2 billion.<sup>87</sup> Because of the mature development of basic services in Canada, most of this growth will be in the emerging telecommunications markets, specifically in wireless and full-service broadband networks.

Canada, with nearly \$22,000 per capita gross domestic product (GDP) in 1992, is a wealthy nation, and many telecommunications firms seek to participate in the Canadian market.<sup>88</sup> The trend toward globalization, made all the more significant in Canada as a result of NAFTA, compels multinational telecommunications firms to develop a Canadian presence. AT&T, MCI, and Sprint have all entered the Canadian market, each with a notably different approach, all confined by Canada's limitation on foreign ownership.

81. See ROBERT W. CRANDALL & LEONARD WAVERMAN, *TALK IS CHEAP: THE PROMISE OF REGULATORY REFORM IN NORTH AMERICAN TELECOMMUNICATIONS* (Brookings Institution, forthcoming 1995).

82. BRUNCOR INC., 1994 ANNUAL REPORT 26 (1995).

83. TELECOM DECISION CRTC 94-19, at 50 (Sept. 16, 1994).

84. ITU WORLD DEVELOPMENT REPORT, *supra* note \_\_, at A-3.

85. BCE INC., 1994 ANNUAL REPORT 20 (1995); Garibaldi & Torres, *supra* note \_\_, at 252.

86. ITU WORLD DEVELOPMENT REPORT, *supra* note \_\_, at A-3.

87. NORTH AMERICAN TELECOMMUNICATIONS ASSOCIATION, 1995 TELECOMMUNICATIONS MARKET REVIEW AND FORECAST 241 (1995).

88. ITU WORLD DEVELOPMENT REPORT, *supra* note \_\_, at A-3.

The Canadian government has decided that competition and market forces should determine the future of the nation's telecommunications industry. The most obvious source of competition is foreign telecommunications firms. The 33.3 percent cap on foreign investment, however, will tend to limit the ability of foreign carriers to operate in Canada on terms sufficiently attractive to induce their entry into the market.

*Telephony.* In June 1993, The Canadian government enacted the Telecommunications Act, which defines Canadian telecommunications policy and authorizes the Canadian Radio-television and Telecommunications Commission (CRTC) to regulate the industry in furtherance of the objectives of this policy.<sup>89</sup> The statute authorizes the CRTC to regulate all telecommunications services provided by Canadian carriers and to forbear from regulation if sufficient competition exists in the marketplace.<sup>90</sup>

The Telecommunications Act specifies eight objectives of the Canadian telecommunications policy:

- (1) to facilitate the orderly development throughout Canada of a telecommunications system that serves to safeguard, enrich and strengthen the social and economic fabric of Canada and its regions;
- (2) to render reliable and affordable telecommunications services of high quality accessible to Canadians in both urban and rural areas in all regions of Canada;
- (3) to enhance the efficiency and competitiveness, at the national and international levels, of Canadian telecommunications;

89. BCE INC., 1993 SEC FORM 20-F, at 9 (1994); Garibaldi & Torres, *supra* note \_\_\_, at 252.

90. NEWTEL ENTERPRISES LTD., 1994 ANNUAL REPORT 17 (1995).

- (4) to promote the use of a Canadian transmission facilities for telecommunications within Canada and between Canada and points outside Canada;
- (5) to foster increased reliance on market forces for the provision of telecommunications services and to ensure that regulation, where required, is efficient and effective;
- (6) to stimulate research and development in Canada in the field of telecommunications and encourage innovation in the provision of telecommunications services;
- (7) to respond to the economic and social requirements of users of telecommunications services; and
- (8) to contribute to the protection of the privacy of persons.<sup>91</sup>

Objective number five really is a means by which the CRTC will attempt to accomplish the other seven objectives. Its significance lies in the fact that it explicitly identifies the Canadian government's recognition of competition as the most efficient force to drive the nation's telecommunications progress.

On September 16, 1994, the CRTC issued Telecom Decision 94-19, setting forth a comprehensive regulatory framework for greater levels of competition throughout the Canadian telecommunications industry.<sup>92</sup> Under the new framework, competition will be permitted in the local service market.<sup>93</sup> Cable television companies, new wireless service providers, resellers, and specialized service providers will all be permitted to provide voice, data, and video services to

91. TELECOM DECISION CRTC 94-19, at 4 (Sept. 16, 1994).

92. *Id.*

93. *Id.* at 33.

local subscribers.<sup>94</sup> In addition, the CRTC will permit telephone companies to carry certain licensed broadcast services, including switched video.<sup>95</sup> Non-facilities-based resellers of telecommunications services are exempt from regulation under the Telecommunications Act, and the CRTC has the authority to exempt as well any class of carriers in a market where effective competition exists.<sup>96</sup>

Canadian law, however, continues to restrict who may compete in the new, more competitive Canadian regulatory regime. Under the Telecommunications Act, a telecommunications common carrier in Canada must be a Canadian corporation, Canadian owned and controlled.<sup>97</sup> The Canadian ownership and control requirement mandates that (1) at least 80 percent of the company's directors must be Canadian citizens, (2) Canadians must beneficially own at least 80 percent of the voting share of the carrier, and (3) the carrier must not otherwise be controlled by non-Canadians.<sup>98</sup> Under regulations adopted pursuant to the Telecommunications Act, entities that qualify as "Canadian" for determination of the 80 percent beneficial ownership requirement include corporations of which Canadians own at least two-thirds of the voting stock.<sup>99</sup> So, in effect, the Canadian foreign ownership restrictions on a telecommunications common carrier require that at least 80 percent of the carrier's board of directors be comprised of Canadian individuals; that direct foreign ownership in the carrier be limited to less than 20 percent; and that ownership in the carrier's parent company be limited to 33.3 percent.

The Director of Investigation and Research of Canada's Bureau of Competition Policy has identified two reasons why the foreign ownership restrictions should be abolished:

First, these restrictions impose costs on the domestic communications industry in terms of limiting access to financial capital resources. Second, barring foreign enterprises leads to a reduced competition in this sector

94. BRUNCOR INC., 1994 ANNUAL REPORT 26 (1995).

95. TELECOM DECISION CRTC 94-19, at 50 (Sept. 16, 1994).

96. BCE INC., 1993 SEC FORM 20-F, at 9 (1994).

97. *Id.*

98. *Id.*

99. *Id.*

relative to other areas of the economy where restrictions do not apply.<sup>100</sup>

The Director also emphasized the critical importance of the availability of investment capital for the construction of advanced telecommunications infrastructure.

Most, if not all, direct investment or non-equity participation by foreign entities in Canada's telecommunications industry has been in the provision of basic long-distance services. For decades, Stentor, an alliance of eleven telecommunications operators, provided long-distance service on an exclusive basis. In 1992, the Canadian government terminated Stentor's monopoly over long-distance services. As of 1995, three telecommunications operators provide fixed-link international long-distance service in Canada. Stentor and Unitel Communications Inc. (Unitel) provide international long-distance services between Canada and both Mexico and the United States.<sup>101</sup> Téléglobe holds a statutory monopoly over international services between Canada and everywhere except the United States or Mexico; Téléglobe's monopoly expires in 1997.<sup>102</sup> BCE Inc. owns 24.4 percent of Téléglobe.<sup>103</sup>

Stentor provides fixed-link domestic long-distance services as well as international. Until 1992, Stentor provided these services on a monopoly basis. Stentor is a working association of eleven companies: British Columbia Telephone, Bell Canada, ED Tel, The Island Telephone Company, The Manitoba Telephone System, Maritime Telephone & Telegraph, New Brunswick Telephone, Newfoundland Telephone, Québec Téléphone, SaskTel, and Telesat.<sup>104</sup> Stentor's members agreed to interconnect their networks to be able to provide their customers integrated communications services. Each member

100. Submission of the Director of Investigation and Research, Bureau of Competition, to the Canadian Radio-television and Telecommunications Commission, Public Notice CRTC 1994-130, Order in Council P.C. 1994-1689, at 39 (Jan. 16, 1995).

101. UNIVERSITY OF COLORADO INTERDISCIPLINARY TELECOMMUNICATIONS PROGRAM, *supra* note \_\_, at 2-15.

102. ITU WORLD DEVELOPMENT REPORT, *supra* note \_\_, at 63.

103. BCE INC., 1993 SEC FORM 20-F, at 9 (1994).

104. Submission of the Stentor Alliance to the Canadian Radio-television and Telecommunications Commission, Public Notice CRTC 94-130, Order in Council P.C. 1994-1689 (Jan. 16, 1995) [hereinafter Stentor Submission].

owns and operates that portion of the network in its region. As of July 1994, after having faced competition for nearly two years, Stentor had 92 percent of the market.<sup>105</sup>

In September 1992, the members of Stentor and MCI formed a strategic alliance to develop and deliver seamless advanced intelligent networks to customers on both sides of the Canada/U.S. border.<sup>106</sup> Neither MCI nor Stentor acquired an equity interest in the other party.

In 1992, the Canadian government authorized Unitel to provide long-distance service, thereby ending Stentor's monopoly. On June 12, 1992, the CRTC granted Unitel the right to provide competitive long-distance service in British Columbia, Ontario, Quebec, New Brunswick, Prince Edward Island, and Nova Scotia.<sup>107</sup> The CRTC also ordered providers of local telephone service to permit Unitel to interconnect with their facilities on a nondiscriminatory basis.<sup>108</sup> In November 1992, Unitel began offering public long-distance voice telephone services in extended calling areas of Montreal, Toronto, and Vancouver.<sup>109</sup>

In two and half years, however, Unitel has succeeded in capturing only 6 percent of the long-distance market—425,000 customers.<sup>110</sup> Unitel posted losses totalling \$220.7 million in 1992 and 1993, and lost \$131.4 million in the first nine months of 1994.<sup>111</sup> Unitel loses approximately \$730,000 each business day and is expected to lose at least \$140 million in 1995.<sup>112</sup>

Unitel, however, has the financial and operational support of a very important shareholder, AT&T. Canadian Pacific Limited, the transport and energy conglomerate, owns 48 percent of Unitel.<sup>113</sup>

105. Bernard Simon, *Canada dials up long-distance network price war*, FIN. TIMES, July 1, 1994, at 23 [hereinafter *Canada dials up*].

106. MCI COMMUNICATIONS CORP., 1993 ANNUAL REPORT 8 (1994).

107. UNIVERSITY OF COLORADO INTERDISCIPLINARY TELECOMMUNICATIONS PROGRAM, *supra* note \_\_, at 2-15.; BCE INC., 1993 SEC FORM 20-F, at 10 (1994).

108. *Id.*

109. *Id.* at 11.

110. Solange De Santis, *Canadian Pacific Grants Option On Unitel Stake*, WALL ST. J., Jan. 13, 1995, at B6.

111. Bernard Simon, *Shareholders set to announce restructuring plans for Unitel*, FIN. TIMES, Jan. 10, 1995, at 21.

112. De Santis, *supra* note \_\_, at B6.

113. CANADIAN PACIFIC LIMITED, 1994 ANNUAL REPORT 35 (1995).

Rogers Communications Inc., Canada's largest cable television operator, owns 29.5 percent.<sup>114</sup> AT&T owns 22.5 percent.<sup>115</sup> Under an amended shareholders' agreement, Rogers had the option to purchase Canadian Pacific's interest in Unitel by April 28, 1995.<sup>116</sup> On April 19, 1995, Rogers declined to exercise the option, saying that the \$146 million purchase price was too high.<sup>117</sup> The plan had been for Rogers to purchase Canadian Pacific's interest and sell approximately 10 percent to AT&T, raising AT&T's share to the maximum foreign interest allowed under Canadian law.<sup>118</sup> Rogers has indicated that it remains interested in participating in Canada's long-distance market and will continue to try to increase its stake in Unitel, but only for a lower price.<sup>119</sup> If Rogers does not exercise its options, each shareholder will have the right to sell its Unitel shares, subject to rights of first refusal of the two other shareholders.<sup>120</sup> Because Unitel has already invested nearly \$1 billion in infrastructure construction, both AT&T and Rogers will likely retain, if not increase, their respective interests in Unitel.<sup>121</sup>

Although Stentor and Unitel are the only two operators that provide fixed-link domestic long-distance services, many companies participate in Canada's long-distance market as resellers. In the three years since Canada's long-distance telephone business was opened to competition, more than 340 companies have entered the long-distance market.<sup>122</sup> Competition has been fierce, with many losers. Two companies folded in January 1995 and more than a dozen others are predicted to do the same during the remainder of 1995.<sup>123</sup> Entrants in the long-distance market have not succeeded in winning much

114. *Id.*

115. *Id.*

116. *Id.*

117. *Rogers Says It Will Not Pursue Stake in Unitel*, N.Y. TIMES, Apr. 20, 1995, at D4.

118. Susan Yellin, *Rogers still has that long-distance feeling; Company will stay in phone market*, OTTAWA CITIZEN, Apr. 29, 1995, at E1.

119. *Id.*

120. CANADIAN PACIFIC LIMITED, 1994 ANNUAL REPORT 35 (1995).

121. Darren Schuettler, *Future control of Canada's Unitel in limbo*, REUTERS, Apr. 21, 1995.

122. Bernard Simon, *Shake-out on the line in Canada—Unitel has been hard hit in the telecoms war* FIN. TIMES, feb.2, 1995, at 30 [hereinafter *Shake-out on the line*].

123. *Id.*

market share from Stentor. As of July 1994, Stentor retained a 92 percent market share.<sup>124</sup> The challengers to the Stentor alliance, however, received a favorable ruling from the CRTC when the agency ruled that, beginning on July 1, 1994, local companies were required to give their competitors equal access to the long-distance market.<sup>125</sup> Thus, the entrants in the long-distance market were freed from a handicap whereby any long-distance customer seeking to use a carrier other than Stentor had to dial an access code of up to seventeen digits.<sup>126</sup>

Sprint Canada is the largest long-distance reseller in Canada.<sup>127</sup> The company provides long-distance services to small and medium-sized businesses in Ontario, Quebec, and British Columbia.<sup>128</sup> To enter the Canadian market, Sprint Inc. chose to acquire an equity stake in an existing operator rather than create its own new Canadian operator. Part of the rationale for its decision was the 33.3 percent foreign ownership restriction. Sprint purchased 25 percent of an existing reseller, then called Call-Net Enterprises Inc., and changed the name to Sprint Canada.<sup>129</sup> Sprint Canada has emerged as one of the more successful upstarts and is constructing its own nationwide fiber-optic network.<sup>130</sup>

ACC TelEnterprises of Toronto is the second largest reseller. ACC provides long-distance voice and data services to business and residential customers in Ontario, Quebec, and British Columbia.<sup>131</sup>

Fonorola is the third largest reseller. It offers voice and data services to a small group of high-volume business customers in Ontario, Quebec, British Columbia, and across the border in Buffalo, New York.<sup>132</sup> Fonorola also offers residential services to employees of its business customers. Fonorola has acquired several struggling

124. Simon, *Canada dials up*, *supra* note \_\_, at 23.

125. *Id.*

126. *Id.*

127. UNIVERSITY OF COLORADO INTERDISCIPLINARY TELECOMMUNICATIONS PROGRAM, *supra* note \_\_, at 2-16.

128. *Id.*

129. Simon, *Shake-out on the line*, *supra* note \_\_, at 30.

130. *Id.*

131. UNIVERSITY OF COLORADO INTERDISCIPLINARY TELECOMMUNICATIONS PROGRAM, *supra* note \_\_, at 2-16.

132. *Id.*

resellers and aims to become a facilities-based long-distance carrier by building a fiber-optic network along Canadian National Railway's rights of way.<sup>133</sup>

All of these competitors are vying to gain a share of Canada's \$5.3 billion long-distance market.<sup>134</sup> AT&T, MCI, and Sprint have particular interest in the near three-quarters of that revenue generated by telecommunications traffic between Canada and the U.S.—a portion of the market that grows at an annual rate of 15 to 30 percent annually.<sup>135</sup> And despite the limited degree of actual competition, the mere threat of competition has provided Canadian consumers with significant benefits. The new competitors have sparked a price war, compelling the Stentor companies to reduce their long-distance rates. Since the CRTC introduced competition to the long-distance market in 1992, both wireline and wireless rates for long-distance services have decreased.<sup>136</sup> In 1994, demand for long-distance telephone service in Canada grew by 10 percent, while the regional telephone companies initiated sharp rate reductions and forced competitors to follow suit.<sup>137</sup>

In September 1994, the CRTC decided that competition in local telephony also would benefit the public interest and that all barriers to entry should be removed.<sup>138</sup> As of 1995, the nine regional telephone companies continue to have a near complete hold on their respective local markets, and competitive entry in the market for local services will remain unlikely until the CRTC allows for rate normalization by the regional telephone companies. Bell Canada estimates that fifteen cents for every minute of long-distance revenue goes to subsidize local service; the cross-subsidy in the U.S. (also expressed in Canadian currency) is about three cents a minute.<sup>139</sup> A Toronto household pays a basic telephone service fee of only \$11.76 per

133. Simon, *Shake-out on the line*, *supra* note \_\_, at 30.

134. *Id.*

135. UNIVERSITY OF COLORADO INTERDISCIPLINARY TELECOMMUNICATIONS PROGRAM, *supra* note \_\_, at 2-18.

136. BCE MOBILE INC., 1994 ANNUAL REPORT 30 (1995).

137. CANADIAN PACIFIC LIMITED, 1994 ANNUAL REPORT 35 (1995).

138. TELECOM DECISION CRTC 94-19, at 33 (Sept. 16, 1994).

139. Simon, *Canada dials up*, *supra* note \_\_, at 23.